

Supreme Court, U. S.
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IN THE
Supreme Court of the United States
OCTOBER TERM, 1976

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No. 75-1871
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GENERAL FOODS CORPORATION, *Petitioner*,

v.

UNITED STATES, *Respondent*.

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PETITIONER'S REPLY BRIEF
—

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PETITIONER'S REPLY BRIEF

This Reply by Petitioner General Foods Corporation is to the Memorandum for the United States in Opposition to General Foods' petition for a writ of certiorari in this case. The Memorandum for the United States incorporates the Memorandum for the United States in Opposition filed in *Boise Cascade Corporation v. United States*, No. 75-1853. In that case a petition for a writ of certiorari is pending on the same issue as is involved herein.*

* Unless otherwise indicated, references to the Memorandum for the United States or to the Respondent's Memorandum are to the Memorandum filed in the *Boise Cascade* case in this Court, as adopted by reference by the Memorandum filed by Respondent United States in this case.

Petitioner General Foods believes that this case presents an important issue which should be resolved by this Court. The Court of Claims in deciding this case ignored completely—did not even refer to or discuss—the legislative history cited by Petitioner. Neither the opinion of the Court of Claims nor Judge Davis' concurring opinion made so much as a single reference to the legislative history cited by Petitioner which indicated the intent of the statute at issue, Section 1232 of the Internal Revenue Code, when that section was enacted by the Congress in 1954. The issue which this Court should address is whether the Court of Claims can ignore the plainly stated Congressional intent at the time of the enactment of Section 1232 and place an entirely different characterization upon that section. In Petitioner's view it should be established by now that the function of the courts is to apply the laws as passed by the Congress and leave to the Congress the changing of the laws.

Respondent in its Memorandum comes to the same conclusion as the Court of Claims, but by a different route. The Court of Claims ignored, without discussing, the plain statements of Congressional intent. The Respondent in its Memorandum (page 4) states that they don't exist: "The Committee reports do not address the question of the tax consequences of income from original issue discount, which is at issue in this case." Compare this statement with the statements in the Senate and House Committee reports quoted at pages 7 and 8 of the Petition: "Under section 117(f) of the present law, when a corporate or Government bond in registered form or with coupons attached is retired the transaction is treated as a sale or exchange.

There is some uncertainty as to the status of *proceeds* in these transactions, i.e., as capital gain or as interest income where the bond or other evidence of indebtedness has been issued at a discount" S. Rep. No. 1622, 83d Cong., 2d Sess. 112 (1954); 3 U.S.C. Cong. & Adm. News 4745 (1954). "Redemption of all bonds and other evidences of indebtedness will receive capital gain or loss treatment on redemption if issued after December 31, 1954, and if they are otherwise capital assets, *except to the extent that the recovery of issue discount is subject to paragraph (2) [Sec. 1232(a)(2)].*" H. Rep. No. 1337, 83d Cong., 2d Sess. A275 (1954); 3 U.S.C. Cong. & Adm. News 4417 (1954). S. Rep. No. 1622, 83d Cong., 2d Sess. 433; 3 U.S.C. Cong. & Adm. News 5076 (1954). (Emphasis supplied.) As above, the Respondent states that these committee reports do not address the tax consequences of original issue discount. Obviously they do.

As set forth in the Petition, Section 1232 of the Internal Revenue Code of 1954 was enacted by the Congress at a time when there was a conflict among court decisions as to whether original issue discount arising from the sale or exchange of bonds or other evidences of indebtedness issued at a discount was taxable as capital gain or ordinary income. Section 1232 resolved this question for the years after 1954. Section 1232 as enacted in 1954 provided that the gain from the sale or exchange of an obligation issued at a discount was gain received in exchange therefor; the original issue discount received from the sale or exchange of bonds held more than six months was specifically declared by Section 1232 to be "gain from the sale or exchange of property which is not a capital asset." The legislative history quoted above plainly

states that the intent of Congress in enacting Section 1232 was to tax the entire gain, including original issue discount, from the sale or exchange of bonds issued at a discount as capital gain except for the original issue discount on bonds held for more than six months. This is the legislative history the Court of Claims ignored.*

Respondent approaches this case as if Section 1232 of the 1954 Code had never been enacted. Respondent seeks to apply general case law and the decision of *United States v. Midland-Ross Corp.*, 381 U.S. 54 (1965), a decision under the 1939 Internal Revenue Code, which had held that under Section 117(f) of the 1939 Code original issue discount was taxable as ordinary income. The *Midland-Ross* case, decided in 1965, finally put to rest the question of the tax treatment of original issue discount under the 1939 Code upon which there was a conflict of decisions in 1954. But in the meantime Section 1232 was enacted to resolve this question for the years after 1954 and that section, not *Midland-Ross*, is controlling in this case. Even in seeking to apply the general tax principles of *Midland-Ross* in the 1954 Code years, Respondent's analysis of those principles is incorrect. Respondent in its Memo-

* Interestingly enough, both the Court of Claims opinion and Judge Davis in his concurring opinion do refer to the statement by Congress in 1969 when it amended Section 1232 which once again made plain the meaning of Section 1232: "[G]ain on the sale or exchange of a bond or other evidence of indebtedness which is a capital asset in the hands of the taxpayer but which has not been held by the taxpayer for more than six months is to be treated as a short-term capital gain as under present law." S.Rep. No. 552, 91st Cong., 1st Sess. 148 (1969); 2 U.S.C. Cong. & Adm. News 2180 (1969). Because this statement of Congressional intent was made subsequent to the enactment of Section 1232, evidently the Court of Claims found it easier to brush aside than the statements of intent made at the time of enactment.

randum (page 4) states that amounts received attributable to original issue discount are not entitled to capital gains treatment "because their source is not a capital asset." In fact the source—the bonds—is a capital asset and Respondent has never disputed this. The question at issue is the tax treatment of the proceeds—the original issue discount—from the source.

CONCLUSION

For the reasons stated herein, and in the Petition, the Petition for writ of certiorari should be granted.

Respectfully submitted,

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